

Allianz Australia Insurance Limited
ABN 15 000 122 850

19 September, 2016

Neil Singleton
Insurance Commissioner
Motor Accidents Insurance Commission
Email: maic@maic.qld.gov.au

Dear Neil,

RE: A Review of Queensland's Compulsory Third Party (CTP) Insurance Scheme

Allianz is pleased participate as an insurer in the successful Queensland CTP Scheme and is an advocate of the Scheme's guiding principles of Affordability, Efficiency, Fairness and Flexibility.

Allianz provides this submission for consideration in the Review of Queensland's CTP Insurance Scheme. Allianz's submission is underpinned by the consideration that Queensland has one of the most affordable CTP schemes in Australia and Scheme features permit efficient competition and customer choice with a socially responsible Vehicle Class Filing Model. Allianz proposes the continuation of Scheme factors that contribute to the scheme's success and suggest enhancements to manage vehicle use innovations, improve claims efficiencies and reduce potential barriers to market entry.

1. Do the guiding principles as outlined represent an appropriate framework to underpin the Scheme? Do you have any comments on how they should be assessed?

Allianz supports the guiding principles as outlined that represent an appropriate framework to underpin the Scheme.

2. Is the current Affordability Index still an appropriate benchmark for deciding when a scheme review needs to be undertaken? Do you have any suggestions of alternative approaches for assessing affordability?

Allianz supports the Affordability Index as an appropriate benchmark for deciding when a scheme review needs to be undertaken. Furthermore, Allianz notes that Queensland's CTP Scheme has performed admirably since its inception and has continued to become more affordable¹. Given Queensland's Scheme is fully community-rated, no segment of the population is subject to higher premiums than any other segment and, therefore, Allianz supports the continued usage of the existing affordability measure.

¹ MAIC, *Discussion Paper: A Review of Queensland's CTP Insurance Scheme*, September 2016

3. On balance, which underwriting model do you believe best meets the guiding principles and why?

Allianz supports a competitive community-rated, private underwriting model as it best meets the guiding principles. Competitive market forces will act to drive premiums for motorists that will contribute to the scheme affordability. Motor Accident Insurance Commission's (MAIC's) market research² identified 84% of respondents are focused on the affordability of premiums, that a competitive market model has been delivering.

Competition encourages insurers to seek efficiency in claims processes and motorists' outcomes as well as innovate to meet customer needs. It has created customer benefits and value beyond legislated CTP coverage, such as at-fault driver protection.

Community rating avoids prejudicing any particular segment of the population, thus eliminating the possibility of adverse community perceptions and the increased propensity for fraud that risk rating creates.

4. Do you believe there is fair price competition in the current Scheme? If not, why not? What changes do you think need to be made to achieve fair price competition if this is seen as a desirable objective?

Allianz believes there is fair price competition in the current Scheme where competition, including the competitive offers provided to motorists, is balanced with the community rating position underpinning the Vehicle Class Filing Model as it is strongly aligned to the affordability guiding principle. Any change disrupting this balance may potentially cause significantly higher prices for some market segments.

Motorists have a plethora of direct monetary benefits as well as non-monetary benefits that insurers provide in addition to vehicle class premium filing. Such benefits are generally increasing over time. Direct monetary benefits provided by insurers to motorists have encompassed gift cards, charitable donations by insurers made on behalf of the motorist and in particular, multi-policy discounts. In the past year, Allianz provided \$1.32M in direct monetary benefits to CTP policy holders to attract and retain their business. These costs are not charged to the CTP portfolio and are fully subsidised by other insurance products. Other insurers have provided rebates and two licence holders have used multi-policy discounts to great competitive advantage, where discounts of up to 15% have been offered on other insurance products if a customer includes CTP in their product bundle.

Non-monetary benefits including at-fault driver protection are offered to motorists at no additional cost. Further, Allianz policy holders may also be eligible for service offerings such as motor fleet risk management services, claims reporting and usage of software systems.

As different insurers compete in the Scheme with different advantages, economies of scale and capability to leverage market share strength in associated business, the Scheme must allow different CTP business strategies to operate and any amendments to the Scheme must not prejudice particular insurer strategies over others. Further, where a variety of successful business strategies is possible, this contributes to lower barriers to entry for new market entrants to improve competition.

As such, Allianz suggests no changes to the current regime with the additional comment of any change considered regarding price competition, must ensure it does not inadvertently

² MAIC, *General Motorist and New Car Buyer Research*, June 2016

prejudice or provide an unnatural competitive advantage to some insurers and not all. Competitive neutrality must be preserved.

Allianz does not recommend consideration of a full risk-rating model; the increased risk of fraud, community concern with segments of motorists being negatively impacted, and significant implementation and ongoing management costs far outweigh any possible benefits and thus should be avoided.

5. In your view, what are the main reasons why motorists do not actively switch CTP insurers? Are there any perceived costs and barriers to switching? Would more active switching lead to increased price competition between insurers?

Allianz does not accept the proposition that motorists do not actively switch CTP insurers. Allianz's experience is that many motorists do not switch as they exercise choice at the point of vehicle purchase, the very affordability of CTP itself provides little economic incentive to switch, and the competitive strategies deployed by insurers to encourage retention presents a significant opportunity cost barrier for switching CTP insurers, especially if the motorist enjoys multi-policy discounts or other bundled product benefits.

Motorists are aware of their ability to switch - 160,131 motorists switched their CTP insurer between 1 July 2015 to 30 June 2016 which equates to approximately 70% of new car registrations in Queensland each year³. Motorists make a conscious selection of their preferred insurer particularly with changes at dealerships requiring the motorist to certify they have independently chosen the specified CTP insurer when purchasing a motor vehicle.

The process to change insurers is well publicised on Department of Transport and Main Roads (DTMR), MAIC and all CTP insurers' websites, when purchasing a motor vehicle from a motor dealer, and through the Transport and Main Roads offices. The change process is quick, simple and efficient with most insurer websites and marketing offers including a 'call to action' where the insurer nomination process is facilitated and efficiently expedited to encourage switching.

Most importantly, motorists are able to exercise their right to switch at any time during the policy lifecycle to take advantage of insurers' switching offers, whilst maintaining portfolio stability for insurers that the switching will occur at the next renewal. Furthermore, once done, the motorist is still able to respond to better offers all the way up to the point of renewal.

However, even if there was greater pricing variability, it is unclear whether it would provide a sufficient economic incentive for motorists to switch. With such an affordable and competitive CTP scheme, for individual motorists, the dollar difference are unlikely to be substantial enough to take action – a 10% difference in price equates to just \$30-40 difference for Class 1 motorists. Such a dollar difference would in many instances not overcome insurer-specific retention strategies and/or a motorists' underlying affiliation to the insurer's brand.

Whilst mechanisms could be introduced to try and artificially force an increase in the insurer switch rate, the costs and associated risks of such mechanisms would need to be carefully assessed.

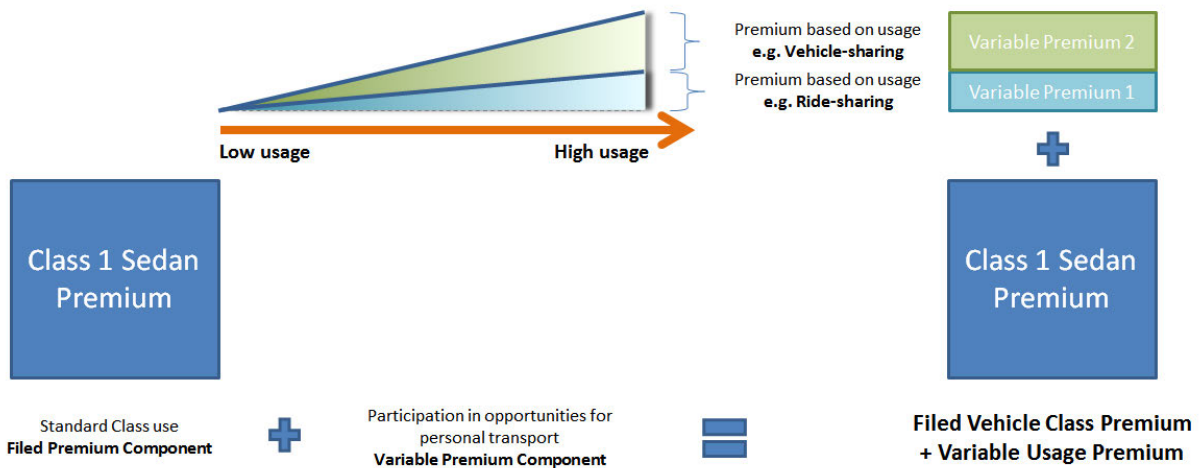
6. Are there any other features of the current Vehicle Class Filing Model that need to be changed to improve the Scheme outcomes?

³ MAIC, *General Motorist and New Car Buyer Research*, June 2016

Allianz supports the existing community-rated Vehicle Class Filing Model and recognises the Model is impacted by the technologically-driven innovations regarding vehicle use and opportunities for personal transport. Examples include ride-sharing services such as Uber and Lyft, whose services were recently legalised in Queensland.

Allianz proposes the incorporation of flexibility within the Vehicle Class Filing Model to address these changes whilst maintaining the social responsibility inherent in the existing model by adding a usage-based variable premium component (e.g. kilometre based) for those engaged in these new opportunities for personal transport.

Proposed approach



The advantages of this approach are manifold.

Motorists who participate in these new opportunities for personal transport are not homogenous in their levels of participation. Further, it is characteristic that participation rates are highly variable as motorists drop in and out. The Uber experience has indicated that within a month of becoming an active Uber driver, 11% of drivers are inactive and within 6 months 30% of users cease driving for Uber⁴. With the pick-up and go nature of participation, Allianz research has found these motorists will have periods of extreme high-use and low-use, varying from full-time to only a couple of hours a week.

A flexible solution is necessary for such variable participation as the approach proposed allows for the continuation of a socially responsible vehicle class filed price for the homogenous component of the risk and a variable pricing component to reflect the motorist's intermittent participation in personal transport services. A similar approach is being implemented in New South Wales including a likely post-registration usage premium payment, facilitated by Uber. We understand Uber has agreed in New South Wales to provide the CTP regulatory agency with data on the Uber-related vehicle use of their drivers in order for CTP premiums to be charged on a usage basis.

The creation of a single vehicle class, for example, a Ride-sharing Class, would limit the ability of MAIC to be flexible enough to move with the speed of innovation as these personal transport service offerings evolve. UberEats exists in Sydney and Melbourne and UberPool is expected to be introduced to Australian market once critical mass is achieved. Further, motorists may participate in multiple permutations for personal transport such as ride-sharing as well as vehicle-sharing and further complexity in vehicle classification will eventuate.

⁴ M.Kosoff, 'Uber just released its first report on its drivers – here are the numbers', *Business Insider*, <http://www.businessinsider.com.au/uber-driver-data-report-2015-1>, (accessed 1 September 2016)

7. Have the changes made to the Scheme in 2010 achieved their intent in ensuring that motorists are aware of their ability to choose their CTP insurer and exercise that choice in the market? Are further changes required, and if so, what?

Allianz considers the changes made to the Scheme in 2010 have substantially achieved their intent in ensuring that motorists are aware of their ability to choose their CTP insurer and exercise choice in the market.

As covered in Question 5, the volume of motorists switching equates to approximately 70% of new car registrations in Queensland each year given the ease and efficiency of the switching process.

Allianz supports the tenet of customer choice and provides CTP scripts to those motor dealers who have an association with Allianz for their commercial insurance needs and who sell Allianz's range of insurance products. In part, the script states "You are able to choose the CTP insurer for your vehicle."

MAIC market research has found ⁵:

- 66% of new car buyers felt satisfied they were able to (or would have been able to if they wanted to) select their preferred CTP insurer
- 73% were aware they were able to select a CTP insurer and 51% of new car buyers reported that in the lead-up to purchasing their new car they did consider the CTP insurer they would select. 84% of registered motor vehicle owners reported that a CTP scheme that has a focus on affordable premiums for the majority of the community is more important to them than a scheme where the focus is on promoting greater price competition between insurers.

The volume of motorists switching insurers and MAIC's research outcomes support the premise that motorists are aware of their ability to choose their CTP insurer and they do exercise that choice – as such, changes are not required.

8. Should CTP insurance be unbundled from vehicle registration? If not, why not? If yes, what would be the perceived benefits?

Allianz does not support the unbundling of CTP insurance from vehicle registration. The bundling of CTP with vehicle registration is simple and efficient, contributing to the affordability objectives, preferred by Queensland motorists, and reduces the risk of claims upon the Nominal Insurer. The minimal benefits of unbundling are far outweighed by the risks and costs to consumers and insurers alike.

The perceived benefit of unbundling is presumably to increase competition derived from ease of choice. It is uncertain whether this would even be achieved through unbundling as customer choice is already inherent in the Scheme.

The unbundling of CTP from vehicle registration will impose an additional transactional cost on all motorists, insurers and the DTMR. Such an imposition will not only have substantial implementation costs, including that of educating motorists, but will also generate ongoing costs that will be incorporated into the Scheme premiums of all motorists, negatively impacting Scheme affordability.

⁵ MAIC, *General Motorist and New Car Buyer Research*, June 2016

Motorists appear to recognise this implicit impost where CTP is unbundled from the Registration process as indicated by the responses received in MAIC's April 2013 Marketing and Communications Research.

Key results of the research indicate that Queensland motorists:

- overwhelmingly prefer a focus on affordable premiums rather than price competition between insurers; and
- prefer paying CTP premiums with their vehicle registration renewals.

Further, the additional transaction required to be carried out by motorists to seek and separately acquire a CTP policy with unbundling, increases the likelihood of motorists driving without the necessary coverage and, hence, of Nominal Defendant claims. To implement controls to mitigate this into the Scheme only further increases the transaction costs of the Scheme.

9. Do you have any comments on the approach used to estimate the economic parameters? Are there alternatives that should be considered?

Allianz supports the current approach used to estimate the risk-free interest rate and wage inflation in the premium setting process. Allianz agrees that the Commonwealth Government bond yield should be maintained as proxy for the risk-free rate and that economic forecasts on Average Weekly Earnings (AWE), such as Deloitte Access Economics, continue to be utilised to obtain an unbiased estimate of wage inflation. It is critical that economic parameters in premium setting are independent, objective and readily observable.

On the superimposed inflation assumption, Allianz recognises MAIC's active involvement in regularly measuring and monitoring the superimposed inflation levels to maintain a sustainable scheme. Allianz suggests that MAIC considers an alternative approach to measuring superimposed inflation as documented by Finity Consulting⁶. This approach enables more robust measurement of superimposed inflation by normalising for differences arising from changes in the composition of claims within an injury severity group over time.

10. Does the current CTP Scheme create barriers to entry that are preventing or deterring new insurers from entering the market? If so, what do you perceive these to be and how should they be addressed?

All classes of insurance involve the allocation of substantial amounts of capital, the retention of employees with expert knowledge and the development of complex systems, thus creating barriers to entry. Queensland's CTP Scheme has barriers to entry that are similar to many other classes of insurance, particularly, long-tail injury classes.

Prior to 2010, there was the perception of increased barriers to entry for intermediated channels, such as motor dealers. The 2010 legislative amendments have eliminated any such barrier to entry.

Given the substantial amounts of capital that insurers must allocate, the primary barrier to entry is the ability to obtain an adequate level of return on this capital. This barrier may be overcome with a strong competition margin in the ceiling price to improve the opportunity of a return to overcome any initial periods of market share build to reach a size where economies

⁶ Cutter et al. *A Claim Pairing Approach to Measuring Superimposed Inflation – A NSW CTP Example*, November 2015

of scale are obtained. Such a measure can assist to reduce the capital investment return assessment conducted by potential market entrants.

11. Should the approach used to determine the allowance for insurer profitability be amended and if so, in what way?

Insurers seek to achieve a level of return in keeping with the expectations of their shareholders having regards to alternative investment opportunities open to them. Insurers that derive inadequate rates of return will suffer a flight of capital, thus constraining their opportunities to participate in markets, such as Queensland's CTP Scheme. Trevor Matthews in his 'Report of the Independent Review of Insurer Profit' dated 15 October 2015, commissioned by SIRA for the New South Wales CTP Scheme, found that insurers are generally targeting a company-wide post-tax return on equity of 15% over the cycle and it is suggested that this would be a useful benchmark in setting CTP premiums. This is equivalent to a profit margin of 12%, which reflects the capital allocation required for the CTP product line and shareholders' expected returns on that capital. This 12% profit margin target at the central premium with a wider range of profit margin between the floor and ceiling premiums could be used for the Queensland CTP Scheme.

There were similar findings from two additional external industry research papers, namely the Actuaries Institute Working Party paper on 'Profit Margins in Regulated General Insurance Markets' in November 2012 and the Deloitte Access Economics paper 'Regulated prices in insurance markets', in June 2014.

12. Should the MAI Act be amended to:

a) introduce a provision to remove the legal defence of inevitable accident?

b) allow children aged 16 years and under the ability to access compensation entitlements under the CTP Scheme even if he or she was at-fault?

a)

Allianz supports the removal of the legal defence of inevitable accident. There are only limited circumstances where the defence of inevitable accident is available. Our experience is the volume of claims where the defence has been invoked is low.

b)

Allianz supports an amendment to the Act to allow children under the age of 16 years, who are at fault, access to compensation entitlements under the CTP Scheme.

13. Do you have any other comments in relation to Scheme coverage?

Allianz has no other comments in relation to Scheme coverage.

14. Should Queensland legislate to require lawyers to disclose details of their fees and the final settlement received by the claimant after all expenses and statutory refunds have been paid? What are the potential implications?

Allianz supports the requirement for lawyers to disclose details of their fees and the final settlement received by the claimant.

The mechanism to capture such data could be easily managed on a quarterly reporting basis via the Personal Injury Register (PIR) which is the same system the insurers currently use to

share data and payments with the Regulator. Understanding the true level of claimant benefit is critical for the Scheme as it is a key scheme performance indicator.

Allianz supports the Regulator requiring access to this information. The Regulator requires this information on claimant benefits to assist the premium setting process. The Regulator should work with the Queensland Law Society who should support this level of transparency. Such a process operates in New South Wales.

15. What other options would improve the transparency of claimant and insurer legal costs under the Scheme?

Affordability and premium setting is a function of claims costs, including legal costs under the Scheme.

Recent claim trends identified by Finity Consulting based on their review of claims experience to 30 June 2016, dated 13 September 2016, supports the need to improve the transparency of legal costs. There has been a material increase in claim frequency of minor severity claims (severity 1) with legal representation in the 2015 and 2016 accident years relative to prior years. This increase is primarily driven by the incidence of pure whiplash claims, which is of lower value relative to all other CTP claims.

Similar trends of increased claims representation for low value minor severity claims were observed in the New South Wales CTP Scheme and was one of the prompts to address legal costs in their 2016 Review. The claim trends observed in Queensland are nascent and there is opportunity to neutralise the underlying legal cost incentives before they are entrenched or become more broadly adopted within the Queensland CTP Scheme, necessitating premium adjustment. The impending crackdown on low severity, legally represented claims arising out of the forthcoming reforms to the New South Wales CTP Scheme will, on past experience, see a redirection of legal effort to other areas, such as Queensland CTP, where opportunities still exist.

Allianz proposes a number of changes to improve the transparency of legal costs under the Scheme. The changes proposed are:

- 1. Exclude CTP from the 50/50 Rule.*

The entitlement to charge up to 50 percent of the damages, as provided by section 347 of the Legal Profession Act 2007, should be abolished for CTP claims. The process lacks transparency, there is limited reporting, if any, and could lead to the erosion of claimant benefits if not controlled – as demonstrated by market research conducted by MAIC in 2014 which revealed that claimants only ultimately retained on average 52 per cent of total settlement amount.

- 2. Increase the claims threshold for regulated legal costs*

The current claims threshold of \$50,000 -indexed to approximately \$71,730 - should be increased to \$100,000, to be indexed annually. In support of this increase, data from Finity Consulting's recent review of claims experience shows that the additional claims driving the increase in frequency, as described above, is on average worth between \$75,000 to \$93,000 (based on the finalisation experience from 2009 to 2016). On average these additional claims will exceed the existing regulated legal costs thresholds, resulting in an increase in legal costs incurred by the Scheme which will place significant pressures on premium.

3. *A cap on legal costs for claims above \$100,000*

Legal costs on claims above the threshold should be capped. Allianz support a legal costs cap of 20% for settlements above \$100,000.

16. Should the role, structure and functions of MAIC be amended in any way, and if so, how and why?

Allianz notes that the Queensland Scheme is amongst the most stable and affordable CTP schemes in Australia and our view is that it would compare favourably with any similar scheme in the world, as such, Allianz does not have suggestions for amendments.

17. Should Queensland's Nominal Defendant (or 'insurer of last resort') Scheme be amended in any way and if so, how?

Allianz does not propose any amendment to the Nominal Defendant Scheme, however, Allianz would participate in the Scheme should there be any changes.

18. Based on your experience with the Queensland CTP Scheme, do you have any other suggestions as to how the objectives of this scheme review could be achieved?

Allianz supports a review of the Funds Management or Trustee Fees payable under the current Scheme. Funds Management Fees, which are fees payable for the settlement funds to be invested on behalf of the claimant, encompasses infant claimants but also serious head injury claimants who lack the mental capacity to manage their settlement funds. Historically, these fees would represent 10-15% of the total settlement. Due to case law over the last decade, these costs have increased significantly and can now represent 30-40% of settlements and in some cases much higher percentages.

New South Wales and Queensland has seen Funds Management costs increase. The increase places upward pressure on premiums and can often delay disbursement of settlement monies due to the complex nature of the assessments.

Allianz proposes a cap on Funds Management, similarly to the way the South Australian CTP Scheme has legislated and removed this head of damage. Allianz proposes a cap of no greater than 20%, which is line with the Queensland Willett v Fletcher Court of Appeal case.

In summary, Allianz believes the Queensland CTP Scheme is fundamentally sound and does not require substantial reforms – it is well placed to meet the Scheme's guiding principles. The enhancements proposed within this submission builds upon the existing Scheme's solid foundation to address market innovations, boost competition and to improve scheme pricing and claims efficiency.

Yours sincerely,



Tony Mobbs
General Manager, CTP